

REPORT BY THE  
AUDITOR GENERAL  
OF CALIFORNIA

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**THE SUPPLEMENTAL DISABILITY  
PAYMENTS PROGRAM SAVES MONEY  
BUT FEW COUNTY EMPLOYEES  
ARE PARTICIPATING**

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REPORT BY THE  
OFFICE OF THE AUDITOR GENERAL  
TO THE  
JOINT LEGISLATIVE AUDIT COMMITTEE

P-049

THE SUPPLEMENTAL DISABILITY PAYMENTS  
PROGRAM SAVES MONEY BUT FEW  
COUNTY EMPLOYEES ARE PARTICIPATING

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P-049

Honorable Art Agnos, Chairman  
Members, Joint Legislative  
Audit Committee  
State Capitol, Room 3151  
Sacramento, California 95814

Dear Mr. Chairman and Members:

The Office of the Auditor General presents its report concerning county retirement systems paying supplemental disability payments in lieu of disability pensions to county employees with service-connected disabilities. We prepared this report in response to Section 7, Chapter 720, Statutes of 1980.

Respectfully submitted,

  
THOMAS W. HAYES  
Auditor General

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## SUMMARY

Since January 1, 1981, the supplemental disability payments program has saved the Los Angeles County Employees Retirement Association more than \$25,000. Moreover, the Los Angeles County Employees Retirement Association will save an additional \$375,000 in disability funds during the working careers of the employees who are receiving supplemental disability payments. Although the program is cost effective, few disabled county employees throughout the State participate in the program. Other county retirement systems could achieve similar savings.

### The Supplemental Disability Payments Program

The County Employees Retirement Law of 1937 authorizes counties to provide disability pensions to county employees who experience service-connected disabilities. Effective January 1, 1981, the Legislature authorized county retirement systems to pay supplemental disability payments in lieu of a disability pension to county employees with service-connected disabilities who accept lower-paying county positions. The supplemental disability payment is equal to the difference between the employee's new salary and the salary for the position the employee held before the disability.

The program enables disabled county employees who return to county employment to receive total compensation that exceeds the payments from a disability pension alone. Moreover, for the county retirement systems, monthly supplemental disability payments are less than payments of a disability pension. Disabled employees, however, are not required to accept county employment, and there is no restriction on the amount of additional noncounty income they may earn if they choose a disability pension instead of supplemental disability payments.

### The Program Is Cost Beneficial

Paying supplemental disability payments in lieu of disability pensions saves money for county retirement systems. For example, between January 1, 1981, and June 30, 1983, the Los Angeles County Employees Retirement Association (association) saved \$25,700 by paying disabled Los Angeles County employees supplemental disability payments instead of disability pensions.

If the employees currently receiving the supplemental disability payments remain in county service, the association will save an additional \$375,000 over the working careers of these employees. This estimate is based on actuarial assumptions described in the report and excludes the costs of rehabilitation services, which are offered to disabled employees whether or not they return to county employment.

### Employees Lack Incentive to Participate

Between January 1, 1981, and June 30, 1983, 1,150 county employees incurred service-connected disabilities in the 20 counties that offer the supplemental disability payments program. Only 20 of these disabled employees, however, have participated in the program.

According to county retirement officials, employees with service-connected disabilities who are capable of performing other duties for the county have no financial incentive to return to county employment; the employees can work for a noncounty employer and receive both a noncounty salary and the disability pension. In most cases, the total compensation from the noncounty job and the disability pension is more than the employee can receive from the lower-paying county job and the supplemental disability payments.

In contrast to the County Employees Retirement Law of 1937, which does not restrict the amount of income a disabled employee may earn in addition to the disability pension, two state retirement systems

may reduce the amount of the disability pension if the disabled employee is earning an income in addition to the pension. Both the Public Employees' Retirement System and the State Teachers' Retirement System have such restrictions on disability pensions.

The supplemental disability payments program was enacted by Chapter 720, Statutes of 1980, and is codified as Section 31725.6 of the California Government Code. This statute is scheduled to expire January 1, 1986.

### Recommendations

To make county retirement systems comparable to the Public Employees' Retirement System and the State Teachers' Retirement System, the Legislature should amend the County Employees Retirement Law of 1937 to require county employees who incur service-connected disabilities and accept disability pensions to report to their retirement system any earnings from a noncounty employer. Further, the Legislature should adopt amendments that require reductions in disability pensions for county employees when their earnings from noncounty employers and the disability pension exceed the current salary for the position the employee held before the disability. These amendments should apply to county employees who incur service-connected disabilities after enactment of the amendments. Such changes may be subject to collective bargaining in those counties that bargain over disability pensions. Finally, because the supplemental disability payments program is cost beneficial, the Legislature should delete the expiration date of January 1, 1986, from Section 31725.6 of the California Government Code.

## INTRODUCTION

The County Employees Retirement Law of 1937 authorizes counties to provide a comprehensive retirement system for county employees. County employees receive a variety of retirement benefits, including retirement payments for length of service in county employment, disability payments for injuries and diseases that incapacitate employees, and death benefit payments for qualifying spouses or children.

To organize a retirement system under the County Employees Retirement Law of 1937, county supervisors must adopt by a four-fifths vote an ordinance establishing a retirement system or the voters must pass such a proposition by a majority vote in a special or general election. County retirement systems are responsible for administration of the retirement laws. Currently, 20 of the State's 58 counties have established retirement systems under the County Employees Retirement Law of 1937. Thirty-five counties contract with the Public Employees' Retirement System, operated by the State to provide retirement benefits for state, county, city, and public agency employees. Two counties operate independent retirement systems, and one county contracts with an insurance company to provide retirement benefits for county employees.

The 20 county retirement systems organized under the County Employees Retirement Law of 1937 had revenues during calendar year 1981 or fiscal year 1981-82 totaling \$1.347 billion, consisting of \$627 million in contributions from counties, \$202 million in



contributions from county employees, and an additional \$518 million from investment income and miscellaneous sources. During the same period, these 20 retirement systems paid retirement and disability benefits totaling \$385 million; the assets of the 20 systems totaled \$6.825 billion.

### Disability Benefits

Under the County Employees Retirement Law of 1937, a county employee is eligible for a disability pension if the employee is permanently unable to perform his/her duties. There are two types of disabilities: service-connected and nonservice-connected. A service-connected disability results from an injury or disease caused substantially by the employee's job. A nonservice-connected disability is the result of injury or disease not related to the employee's job. To be eligible for a disability pension, an employee need not be totally and permanently disabled or incapable of performing other forms of work.

An employee with a service-connected disability receives an annual disability pension equal to one-half of the employee's final compensation, payable monthly. The counties determine an employee's final compensation using either the highest annual earnings during any one-year period or the highest average earnings over any three-year period. The County Employees Retirement Law of 1937 does not require a reduction of the disability pension if the disabled employee is earning an income in addition to the pension.

### Supplemental Disability Payments

In 1980, the Legislature enacted Section 31725.6 of the California Government Code (Chapter 720, Statutes of 1980) which requires county retirement systems to refer an employee with a service-connected disability to a rehabilitation representative to determine if the employee is capable of performing other job duties. The representative determines whether rehabilitation services would enable the employee to become qualified to perform the duties of another county position and consults with county agencies to determine what positions, if any, would be compatible with the employee's aptitudes, interests, and abilities. Rehabilitation services are services such as counseling and training that are reasonably necessary to restore an employee to employment.

If the representative determines that the employee could return to county service in another position, the representative develops a rehabilitation plan that describes how the employee may be able to return to employment. The rehabilitation plan must define the responsibilities of the employee and the county in implementing the plan. When the rehabilitation plan is completed, the representative submits the plan to the employee and the county for their concurrence.

Neither the employee nor the county is required to accept the rehabilitation plan. Further, the employee is not required to accept other county employment and may refuse rehabilitation services that may enable the employee to return to employment. Moreover, even if the

employee accepts the rehabilitation services, the employee may seek and accept noncounty employment without incurring a reduction in the employee's disability pension. The employee is not required to report earnings to the county retirement system.

If, however, both the employee and the county accept the rehabilitation plan, the representative submits the plan to the Division of Industrial Accidents, in the Department of Industrial Relations, for its approval pursuant to Section 139.5 of the Labor Code. The Division of Industrial Accidents reviews the rehabilitation plan to ensure that the plan complies with rehabilitation laws and regulations. After the division approves the rehabilitation plan, the representative notifies the retirement system that the county either is proceeding to implement the approved plan or has subsequently determined that it is unable to provide a position in county service compatible with the rehabilitation plan.

If the county offers the employee a position specified in the approved rehabilitation plan within one year from the date that the employee became eligible for a disability pension, the employee must report for duty in the new position. If the employee refuses the position, the county may apply to the retirement system to have the employee's disability pension discontinued. If the retirement system determines that the employee's reason for refusing the position is not reasonable, the employee's disability pension may be terminated.

Section 31725.6 authorizes county retirement systems to pay supplemental disability payments to county employees with service-connected disabilities if the employees accept lower-paying county positions instead of disability pensions. The supplemental disability payment is equal to the difference between the salary for the position the employee held before the disability and the salary earned from the lower-paying county position; the supplemental disability payment cannot be larger than the disability pension payment that the disabled employee could receive. The supplemental disability payment is adjusted annually to ensure that the employee's total compensation is equivalent to the current salary for the position the employee held before the disability occurred.

Thus, under Section 31725.6, a disabled county employee who accepts a lower-paying county position can receive both salary and supplemental disability payments that, in total, provide the employee with compensation that is higher than the employee's disability pension alone. County retirement systems, in turn, can provide supplemental disability payments that are less than disability pension payments, and counties are enabled to provide continued employment to their disabled employees and receive continued services from these employees. Conversely, a disabled employee who accepts a disability pension and finds noncounty employment may receive income higher than that possible under the supplemental disability payments program.

Section 31725.6 of the California Government Code is scheduled to expire on January 1, 1986.

#### SCOPE AND METHODOLOGY

We conducted this review pursuant to Section 7 of Chapter 720, Statutes of 1980, which requires the Auditor General to report to the Legislature on the costs and savings of paying supplemental disability payments for service-connected disabilities under Section 31725.6 of the California Government Code. Our review excluded payments for disabilities that were not service-connected. Our review covers the period since January 1, 1981, the effective date of Section 31725.6.

In preparing this report, we contacted the 20 retirement systems that were established under the County Employees Retirement Law of 1937 to determine the number of county employees who have been granted service-connected disability benefits since January 1, 1981. We also determined the number of county employees who have participated in the supplemental disability payments program under Section 31725.6.

We also visited two agencies of Los Angeles County: the Los Angeles County Employees Retirement Association and the Rehabilitation Services Bureau of the Department of Personnel. We selected Los Angeles County because nearly two-thirds of the county employees in the State who have service-connected disabilities and are receiving supplemental disability payments are from Los Angeles County.

In Los Angeles County, we reviewed the records of these disabled county employees to determine the reasons for their disabilities and the amount of the supplemental disability funds paid to them. We also determined the amount of the disability pension that each employee would have received if the employee had not chosen to accept a lower-paying county position and the supplemental disability payments.

To compare the disability benefits available to county employees with disability benefits available to state employees and county employees covered by a state retirement system, we reviewed the disability program available to employees under two state retirement systems: the Public Employees' Retirement System and the State Teachers' Retirement System.

We consulted the actuarial staff at the Public Employees' Retirement System to develop a formula for estimating the potential future savings that the Los Angeles County Employees Retirement Association will experience as a result of paying supplemental disability payments in lieu of disability pensions. We assumed that employees who are receiving supplemental disability payments will remain in the county positions they now hold. Also, we assumed that the disability pensions will increase at an annual rate of 3 percent. In developing our estimate of future savings for the Los Angeles County Employees Retirement Association, we used the following assumptions developed by the actuarial firm of Towers, Perrin, Forster & Crosby: an annual interest rate of 8 percent and an annual salary increase of 6 percent. The actuarial firm

also provided the probabilities that the employees would retire, become further disabled, or die while receiving supplemental disability payments.

In preparing this report, we discussed our analyses with and considered the comments of officials from the Los Angeles County Employees Retirement Association and the Rehabilitation Services Bureau of the Los Angeles County Department of Personnel. We also discussed our analyses with representatives of the other county retirement systems and considered their comments in preparing this report. Lastly, we discussed our analyses with officials in the Department of Industrial Relations and considered their comments.

## AUDIT RESULTS

### THE SUPPLEMENTAL DISABILITY PAYMENTS PROGRAM FOR COUNTY EMPLOYEES IS COST EFFECTIVE BUT UNDERUTILIZED

Only 20 of the 1,150 county employees who incurred service-connected disabilities since January 1, 1981, are working in lower-paying county positions and receiving supplemental disability payments in lieu of disability pensions. Although few county employees are participating, the supplemental disability payments program saves money for the county retirement systems. Between January 1, 1981, and June 30, 1983, the Los Angeles County Employees Retirement Association (association) saved \$25,700 in disability payments. Furthermore, the association will save an additional \$375,000 over the working careers of the current disabled employees and would save additional money if more employees accept lower-paying county positions and supplemental disability payments in lieu of disability pensions. Many county retirement officials state that few disabled employees participate because the program lacks financial incentives for the employees. In contrast to the County Employees Retirement Law of 1937, state disability programs may reduce the disability pension if the disabled employee earns an income in addition to the pension.



Few Disabled County Employees  
Participate in the Supplemental  
Disability Payments Program

Between January 1, 1981, when Section 31725.6 of the California Government Code became effective, and June 30, 1983, the 20 county retirement systems that operate under the provisions of the County Employees Retirement Law of 1937 paid disability benefits to 1,150 county employees who were granted service-connected disabilities during this period. However, only 20 county employees with service-connected disabilities participated in the supplemental disability payments program. Table 1 presents the results of our survey of the 20 county retirement systems; the table shows the number of employees with service-connected disabilities and the number of employees participating in the supplemental disability payments program.

TABLE 1

EMPLOYEES WITH SERVICE-CONNECTED DISABILITIES  
AND EMPLOYEES PARTICIPATING IN THE  
SUPPLEMENTAL DISABILITY PAYMENTS PROGRAM  
BETWEEN JANUARY 1, 1981 AND JUNE 30, 1983

<u>County</u>	<u>Employees With Service-Connected Disabilities</u>	<u>Employees Participating in the Supplemental Disability Payments Program</u>
Alameda	7	0
Contra Costa	42	0
Fresno	6	0
Imperial	7	0
Kern	42	0
Los Angeles	762	12
Marin	18	1
Mendocino	7	0
Merced	7	0
Orange	85	0
Sacramento	27	0
San Bernardino	35	0
San Diego	45	0
San Joaquin	5	0
San Mateo	4	3
Santa Barbara	8	1
Sonoma	15	1
Stanislaus	4	0
Tulare	5	1
Ventura	<u>19</u>	<u>1</u>
Total	<u>1,150</u>	<u>20</u>

The Supplemental Disability  
Payments Program Is Cost Beneficial

Based on our review of records for county employees with service-connected disabilities in Los Angeles County, we conclude that paying supplemental disability payments saves money for county retirement systems. In addition, if more employees accept lower-paying county

positions and receive supplemental disability payments, the county retirement systems will save additional money.

Twelve disabled employees received supplemental disability payments from the Los Angeles County Employees Retirement Association. The 12 employees in Los Angeles County were disabled as a result of service-connected injuries such as back or leg injuries, or other disabling conditions such as mental illness. Two of the 12 employees have retired. The ages of the 10 disabled employees still working for the county range from 34 to 60 years.

The disabled employees in Los Angeles County who accepted lower-paying positions since the enactment of Section 31725.6 have received supplemental disability payments for an average of nearly 9 months, with a range from .5 months to 19 months. By paying supplemental disability payments to these employees, the association saved \$25,700 in disability payments between January 1, 1981, and June 30, 1983. The savings is the difference between the amount of disability pension the association would have paid to the disabled employees and the amount that the association paid in supplemental disability payments. The savings range from \$200 to \$8,100 per disabled employee.

In calculating the savings to the association, we excluded the costs of rehabilitation services that enable the disabled employees to return to employment. Counties must provide rehabilitation services to an employee with a service-connected disability if the employee will

benefit from rehabilitation services. Since counties must provide rehabilitation services to qualified employees whether or not the employees seek county employment, the costs of rehabilitation services do not affect the savings that result from paying supplemental disability payments.

The following example illustrates the savings to the association as a result of supplemental disability payments. A county employee, who worked as a security officer until he was disabled because of a service-connected injury to his shoulder, accepted a lower-paying county position and supplemental disability payments. The employee earned \$1,723 per month as a security officer before the disability occurred. After the disability, the employee received rehabilitation services that enabled him to accept a lower-paying position as a laboratory assistant. The employee's salary as a laboratory assistant was \$1,212 per month. The monthly supplemental disability payment was \$511, the difference between his previous monthly salary of \$1,723 as a security officer and his new lower salary of \$1,212. Had the employee chosen not to accept the lower-paying county position and the supplemental disability payments, he would have received a disability pension of \$862 per month, one-half of his final compensation. Thus, by providing this employee supplemental disability payments instead of a disability pension, the association saves money and the employee's total compensation equals the salary he received before the disability. At June 30, 1983, this employee had been receiving supplemental disability payments for five months, and the association had saved \$1,600 in disability payments.

Furthermore, the association will save money by paying the supplemental disability payments to this employee and other county employees who receive the supplemental disability payments instead of disability pensions. We estimate that the association will save \$375,000 over the working careers of the 10 employees who are currently receiving supplemental disability payments. The future savings for each employee range from \$1,500 to \$110,000. This estimate of future savings was developed with the assistance of the actuarial staff of the Public Employees' Retirement System. The estimated savings represent the current value of future savings during the working careers of the employees, reduced by an interest discount factor. The future savings is adjusted to reflect the probabilities that each employee will retire, become further disabled, or die while receiving supplemental disability payments. We also adjusted the estimated savings to reflect the cost-of-living increases during the working careers of the employees.

Further, the association will save additional money if more employees with service-connected disabilities accept lower-paying county positions and the supplemental disability payments. Currently, the association has eight employees applying for service-connected disabilities who wish to participate in the supplemental disability payments program.

The expiration of Section 31725.6 on January 1, 1986, would end future savings; the county retirement systems will be unable to pay supplemental disability payments in lieu of disability pensions to employees who become disabled after the law expires.

### Employees Have No Financial Incentive to Accept Supplemental Disability Payments

Most county retirement officials that we surveyed stated that few disabled employees are participating in the supplemental disability payments program because this program provides little financial incentive to do so. These officials stated that a disabled employee who is capable of performing other duties can earn a salary from a noncounty employer and also receive the disability pension of one-half of the employee's final county compensation. In most cases, the noncounty salary and the disability pension are larger than the combined supplemental disability payment and the salary from a lower-paying county position.

For example, an employee who earns \$2,000 per month and becomes disabled with a service-connected injury is eligible for a disability pension of \$1,000 per month, one-half of the employee's final compensation. If the employee earns a salary of \$1,500 per month from a noncounty employer, the employee would receive a total of \$2,500 per month--\$1,000 from the disability pension and \$1,500 from the noncounty employer. On the other hand, if the employee accepts a \$1,500 per month county position, the employee would receive \$2,000 per month--the \$1,500 county salary and \$500 for the supplemental disability payment. As this example shows, this hypothetical employee would have no financial incentive to work for the county in a lower-paying position even with the supplemental disability payment; the employee receives \$500 more per month by not working for the county.

## State Disability Programs Restrict Earnings

In contrast to the County Employees Retirement Law of 1937, which does not restrict the amount of income disabled county employees may earn in addition to their disability pension, both the Public Employees' Retirement System (PERS) and the State Teachers' Retirement System place restrictions on disabled employees who are receiving disability pensions. Both retirement systems may reduce the amount of the disability pension in certain instances if the disabled employee is earning an income in addition to the pension. For example, except for certain employees such as highway patrolmen and correction officers, and employees who have reached the minimum age for a service retirement, the PERS requires disabled employees who are employed by a "non-PERS employer" (any governmental agency or private entity that does not participate in the Public Employees' Retirement System), to report earnings from this employment to the PERS. The PERS reduces the amount of the disability pension if the sum of the employee's salary from the non-PERS employer and the portion of the disability pension not paid by the employee's contributions is larger than the current salary for the position that the disabled employee held before the disability retirement. The PERS restrictions on earnings also apply to the 35 counties that contract with the PERS to provide disability benefits.

The State Teachers' Retirement System (STRS) permits disabled employees to accept any employment. However, the STRS will reduce the disability pension for any month in which the disabled employee's

earnings and the disability pension exceed the salary for the position, adjusted for inflation, that the employee held before becoming disabled. Also, the STRS will terminate the disability pension if the employee's average earnings from employment for any continuous six-month period equals two-thirds of the salary for the position, adjusted for inflation, that the employee held before the disability.

### CONCLUSION

Paying supplemental disability payments to eligible employees with service-connected disabilities is cost beneficial to county retirement systems. However, only 20 of 1,150 disabled employees eligible for supplemental disability payments under Section 31725.6 of the California Government Code are participating in the program. County retirement officials stated that disabled county employees who are capable of working do not want to work for the counties because they can earn more money by working for a noncounty employer while receiving a county disability pension. In contrast, state disability programs may reduce the disability pension if the disabled employee is earning an income in addition to the pension.




## RECOMMENDATION

To make county retirement systems comparable with the Public Employees' Retirement System and the State Teachers' Retirement System, the Legislature should amend the County Employees Retirement Law of 1937 to require county employees with service-connected disabilities to report to their county retirement system any earnings from a noncounty employer. Further, the Legislature should adopt amendments that require county retirement systems to reduce the disability pension of employees whose total income from noncounty employers and the disability pension is larger than the current salary for the position the employee held before the disability. These amendments should apply to those county employees who incur service-connected disabilities after the amendments are enacted. Such changes may be subject to collective bargaining in those counties that bargain over disability pensions. Finally, because county retirement systems have saved money by paying supplemental disability payments, the Legislature should delete the expiration date of January 1, 1986, from Section 31725.6 of the California Government Code.

We conducted this review under the authority vested in the Auditor General by Section 10500 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,

  
THOMAS W. HAYES  
Auditor General

Date: December 27, 1983

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cc: Members of the Legislature  
Office of the Governor  
Office of the Lieutenant Governor  
State Controller  
Legislative Analyst  
Director of Finance  
Assembly Office of Research  
Senate Office of Research  
Assembly Majority/Minority Consultants  
Senate Majority/Minority Consultants  
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